SUPREME COURT, U. S.
OCT 23 1973
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In The

Supreme Court of the United States

October Term, 1973

No. 73-677

BRIGADOON SCOTCH DISTRIBUTORS, LTD., and MILBANK TRADING CO., INC.,

Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Petitioners,

-against-

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this case on June 7, 1973. Petitioners' motion for rehearing was denied by an order dated July 24, 1973.

OPINIONS BELOW

The opinion of the Court of Appeals, not yet officially reported, and the two opinions below of the District Court for the Southern District of New York, Tenney *J.*, appear in the appendix hereto.

JURISDICTION

The judgment of the Court of Appeals for the Second Circuit was entered on June 7, 1973. A timely petition for rehearing *en banc* was filed on June 21, 1973, and denied by order dated and filed on July 24, 1973. This petition for certiorari was filed within 90 days after the latter date. This Court's jurisdiction is invoked under 28 U.S. Code Sec. 1254(1).

QUESTIONS PRESENTED

(1) Was it a violation of the Fourth Amendment and of the interpretation thereof in *See v. Seattle*, 387 U.S. 541 (1967), for the Circuit Court below to hold that where (A) a federal regulatory agency (here the SEC) applies to a federal district court for an order enforcing a subpoena *duces tecum* seeking information contained in private business records and files and (B) the agency merely alleges that the subpoena was issued for a "legitimate purpose" and for the particular purpose, among others, of obtaining so-called "jurisdictional facts" to enable the agency to make an "initial determination" as to whether or not the agency has statutory jurisdiction over the person served with the subpoena, then, in such a case, the provision of the Fourth Amendment that "no Warrants shall issue, but upon probable cause" and the interpretation of that provision in *See v. Seattle* do not require the agency to make to the district court any factual showing at all, however slight, of "probable cause" or reasonable justification for conduct of the investigation and intrusion by court process into the private files and records of the respondent?

(2) Was it error and a violation of petitioners' Fourth Amendment rights for the court below to hold "that an agency need not demonstrate facts showing either the probability of coverage under the [pertinent regulatory] statute or the likelihood of violation of the statute to secure enforcement of a subpoena?

Questions Involved

(3) Was it error and a violation of petitioners' Fourth Amendment rights for the court below to hold, that the "probable cause" requirement of the Fourth Amendment is, in effect, abrogated or suspended or otherwise inapplicable to administrative subpoenas *duces tecum* seeking so-called "jurisdictional facts" with respect to possible statutory "coverage" or regulatory jurisdiction of the agency over the business of the respondent, with the result that the district court asked to issue a subpoena enforcement order may not require the agency to show any facts at all upon which issuance of the subpoena was based as a condition to issuance of the order; but, instead, that court must simply "rubber stamp" the agency's application as written, without even the slightest showing having been made of any factual basis for the invasion by subpoena and court order of the privacy of the respondent's business records?

(4) Is there a direct and irreconcilable conflict between (A) the holding of the Second Circuit below in this case and the related holding of that court in SEC *v. Wall Street Transcript Corp.*, 422 F.2d 1371 (2d Cir. 1970), *cert. denied*, 398 U.S. 958 (1970), (that no showing of "probable cause" need be made under the Fourth Amendment for enforcement by the SEC through judicial process of a subpoena for business records seeking "jurisdictional facts") and (B) that of the Supreme Court in *See v. Seattle*, 387 U.S. 541 (1967), (that the "probable cause" requirement of the Fourth Amendment is applicable to "administrative agencies at all levels of government," *i.e.*, both state and federal, and "to a broad range of investigations," including, "inspection of the structure in which a business is housed, as in this case, or inspection of business products, *or a perusal of financial books and records*" [387 U.S. at 544, emphasis supplied])?

(5) Was it error for the court below to hold that the holding of this Court in *See v. Seattle*, *supra*, is limited in its application to cases in which "there was governmental entry onto private property" and does not apply to cases involving "an administrative subpoena for the production of books and

records" -- despite the plain language to the contrary in *See v. Seattle* set forth in the second quotation above?

(6) Is there a direct and irreconcilable conflict between the holding of the Second Circuit in *Newark & Co. v. Wirtz*, 330 F.2d 576, 578 (2d Cir. 1964) (that (A) the SEC may conduct, by district court subpoena enforcement order and *without any showing of factual "probable cause"* in so-called "initial determination of coverage" situation, "simultaneously . . . a full inquiry into *both* potential coverage *and* potential [substantive] violations . . . [and (B)] in aid of such investigations the Commission may issue subpoenas which will produce information on both issues" [op., p. 4012]) and that of the Supreme Court three years later in *See v. Seattle*, *supra*, (that the "probable cause" requirement *applies* in such subpoena situations, with no exception indicated for "initial determination" cases)?

STATUTES AND REGULATIONS INVOLVED

(1) *Amendment IV to the Constitution*

> "The right of the people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures, shall not be violated, and no Warrants shall issue, but upon probable cause, supported by Oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized."

(2) *Section 20(a) of the Securities Act of 1933* ("Securities Act"), 15 U.S.C. Sec. 77t(a)

> "Section 20. (a) Whenever it shall appear to the Commission, either upon complaint or otherwise, that the provisions of this title, or of any rule or regulation prescribed under authority thereof, have been or are about to be violated, it may, in its

discretion, either require or permit such person to file with it a statement in writing, under oath, or otherwise, as to all the facts and circumstances concerning the subject matter which it believes to be in the public interest to investigate, and may investigate such facts."

(3) *Sections 2(1), 5(a), 5(c), 17(a) and 19(b) of the Securities Act*

"Section 2. When used in this title, unless the context otherwise requires--

(1) The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a 'security' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

"Section 5. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly--

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale."

"(c) It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 8."

"Section 17. (a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly--

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser."

"Section 19. (b) For the purpose of all investigations which, in the opinion of the Commission, are necessary and proper for the enforcement of this title, any member of the Commission or any officer or officers designated by it are empowered to administer oaths and affirmations, subpoena witnesses, take evidence, and require the production of any books, papers, or other documents which the Commission deems relevant or material to the inquiry. Such attendance of witnesses and the

production of such documentary evidence may be required from any place in the United States or any Territory at any designated place of hearing."

STATEMENT OF THE CASE

The pertinent facts involved are set forth accurately and at length in the opinion below (pp. 4000-4005 thereof) included in the Appendix hereto.

In brief, those facts are as follows. The respondent Securities and Exchange Commission ("SEC" or the "Commission") issued and served identical administrative subpoenas *duces tecum* upon petitioners Brigadoon Scotch Distributing Co. ("Brigadoon") and Milbank Trading Co., Inc. ("Milbank") demanding production at the Commission's New York Regional Office of eight categories of documents. Both subpoenas were issued on April 14, 1971, and both were issued pursuant to an Investigative Order issued by the Commission on February 14, 1971, which was purportedly authorized by Section 20(a) of the Securities Act. Section 20(a) authorizes the SEC to investigate into possible violations of the federal securities law. Claiming authority under Section 19(b) of the Securities Act, the Investigative Order directed the Commission's staff to conduct a private investigation to determine whether or not certain named persons (including both Brigadoon and Milbank) or others had engaged or were about to engage in acts or practices in connection with the purchase and sale of "whisky warehouse receipts."

The petitioners responded with different amounts of information, but neither complied fully or to the satisfaction of the SEC with the subpoenas. As a result, the SEC commenced the subpoena enforcement proceedings involved in this case.

In support of its application to District Judge Tenney for a court order enforcing the instant subpoenas *duces tecum*,

the SEC submitted only the following: (1) a copy of the Commission's Investigative Order to its staff; (2) a copy of each of the three subpoenas served on the respondents; (3) a statement in the notice of application that the respondents had failed to comply with the subpoenas; and (4) a memorandum of law dated January 25, 1972. No presentation or showing was made to the district court, whether by affidavit or otherwise, of *any facts* possessed by the Commission or its staff to justify or to demonstrate "probable cause" for either (a) issuance of the Investigative Order by the Commission or (b) issuance of the instant subpoenas by a staff attorney of the SEC to the respondents.

The petitioners opposed the SEC's application to the district court on jurisdictional grounds, *i.e.*: (1) the Investigative Order was not authorized by Section 20(a) of the Securities Act; (2) the directive in the Investigative Order was not authorized by Section 19(b) of that Act; (3) the things offered and sold by the defendants are not "securities" within the meaning of Section 2(1) of that Act and the SEC had neither a reasonable belief that they were securities nor any facts upon which such a reasonable belief could be based; (4) those things are not, as a matter of fact or law, "warehouse receipts"; (5) the court therefore lacked jurisdiction of the proceeding and the SEC lacked both statutory authority and a factual basis for commencing it; (6) the SEC had presented to the court absolutely no facts whatever, whether by affidavit or otherwise, in support of its application upon which the district court could reasonably exercise its discretion and determine whether or not either the Investigative Order or the instant subpoenas was arbitrarily issued or the application to the court well-founded; and (7) that, in the absence of any factual showing at all to support the SEC's request for judicial relief, issuance by the district court of the requested subpoena enforcement order would violate petitioners' Fourth Amendment rights as set forth in *See v. Seattle*, *supra*, and related cases, and fundamental principles of equity.

Statement of the Case

In its opinion, the district court held that those items of the subpoenas (1 through 6) which it deemed relevant to the question of whether or not petitioners were engaged in the sale of "securities" within the meaning of Section 2(1) should be produced, but that other items (7 and 8) should not be produced until such later time as the SEC could demonstrate to the satisfaction of the court that, as a matter of fact and law, petitioners were selling "securities" as defined in the federal securities laws. *SEC v. Brigadoon Scotch Distributing Co.*_____ F. Supp. ____ *(S.D.N.Y., 1/10/73, Tenney, J.), CCH* Fed. *Sec. L. Rep., 72-73 Decisions* Para. 93, 731. In addition, the district court, in the proper exercise of its discretion, required the Commission to state a disclaimer or explanation prescribed by the court to any person whose identity it should obtain from petitioners and from whom it should seek information pursuant to its investigation. Basically, such persons would be customers, salesmen and banks of the petitioners, and the court sought to protect petitioners against destruction of their businesses by the investigative efforts of the Commission's staff.

In its decision below, the Second Circuit granted the SEC everything it had requested and reversed every aspect of the district court's opinion which favored the petitioners or sought to protect them either procedurally or substantively in any way. The district court's holding as to the immediate enforceability of items 1 through 6 of the subpoenas was affirmed. In all other respects, the decision of the district court was reversed, *SEC v. Brigadoon Scotch Distributing Co.*, F.2d (2d Cir., 6/7/73 CCH *Fed. Sec. L. Rep., Curr. Vol.* Para. 94, 017. Petitioners of course claim that the prospective and purely procedural aspects of the district court's ruling were within its discretion and involved neither an abuse of discretion nor any error of law. Consequently, they submit that the circuit court's reversal of those aspects of the district court's opinion constituted reversible error.

REASONS FOR GRANTING THE WRIT

POINT I

The decision below violates petitioners' constitutional rights under the Fourth Amendment and places that and related decisions by the Second Circuit in direct conflict with the holding of this court in See v. Seattle, 387 U.S. 541 (1967).

The Fourth Amendment provides that "no Warrants shall issue, but upon probable cause." In *See v. Seattle* this Court held: (1) that "administrative agency subpoenas of corporate books or records" constitute "Warrants" within the meaning of the Fourth and Fourteenth Amendments; (2) that, consequently, the "probable cause" requirement of the Fourth Amendment applies to "administrative agencies at all levels of government," *i.e.*, both state and federal, and "to a broad range of investigations," including "inspection of the structure in which a business is housed, as in this case, or inspection of business products, or a perusal of financial books and records" (387 U.S. at 544); and (3) that the "probable cause" test is "a flexible standard of reasonableness that takes into account the public need for effective enforcement of the particular regulation involved" together with the constitutional rights and property or business interests of the respondent, but which requires, nonetheless, in every case, that an appropriate and significant *factual* showing of "cause" be made by the investigative agency to justify judicial enforcement of the particular warrant or subpoena involved.

Absolutely no factual showing of any kind whatsoever by way of "probable cause" was made by the SEC in its application to the district court in this case for a subpoena enforcement order. That fact was clearly conceded by the circuit court below in its opinion. But despite that fact, the court below held that the instant subpoenas must be enforced in full and without any of the protective measures adopted by the district court.

Reasons for Granting the Writ

Thus the court below found and held that no showing of factual "probable cause" had been made to the district court sufficient to satisfy the Fourth Amendment test, but it held that the subpoenas must be enforced by the district court anyway, without any such showing having been made. In so holding, the circuit court, ruled, in effect, that the Fourth Amendment's "probable cause" requirement and the constitutional protection thereby afforded is erased or abrogated in every subpoena *duces tecum* case in which the SEC (or any other federal agency cloaked with subpoena powers) merely alleges a statutory purpose for the investigation and claims, quite nakedly, that the subpoena was issued for the purpose of gathering so-called "jurisdictional facts." It did so because the district court is (A) required by the circuit court's holding to accept at face value (i) the "good faith" of the government investigator who issued the subpoena and seeks to enforce it and (ii) the truth and existence of his stated purpose and (B) precluded from requiring any *objective*, factual proof or "probable cause" to show that there is some good reason to conduct the investigation and to violate the privacy of the respondent's business records. In the absence of a meaningful *objective* standard for judging the propriety and necessity of the subpoena, the district courts in the Second Circuit will be reduced hereafter, in these subpoena enforcement proceedings, to serving as little more than ministerial "rubber stamps" for the regulatory agencies, required to issue subpoena enforcement orders automatically on demand and without any meaningful, critical evaluation based upon relevant facts — for the agency is not required to show any facts, as it in fact did not in this case.

The opinion of the Second Circuit below and its related opinions to the same effect in *S.E.C. v. Wall Street Transcript Corp.*, 422 F.2d 1371 (2d Cir. 1970), *cert. denied*, 398 U.S. 958 (1970), and *Newmark & Co. v. Wirtz*, 330 F.2d 576, 578 (2d Cir. 1964), are therefore in direct and irreconcilable conflict with the plain mandate of the Fourth Amendment and with the holding of this Court in *See v. Seattle*, *supra*.

Reasons for Granting the Writ

That conflict justifies the grant of certiorari to review the judgment below.

In its opinion below the circuit court held:

(i) that, where (A) a federal regulatory agency (here the SEC) applies to a federal district court for an order enforcing compliance with a subpoena *duces tecum* seeking information contained in private business records and files and (B) the agency alleges that the subpoena was issued for a "legitimate purpose" and for the particular purpose, among others, of obtaining "jurisdictional facts" to enable the agency to make an "initial determination" as to whether or not the agency has statutory jurisdiction over the person served with the subpoena, then, in such a case, the provision of the Fourth Amendment that "no Warrants shall issue, but upon probable cause" and the interpretation of that provision in *See v. Seattle*, 387 U.S. 541 (1967), do not require the agency to make to the district court any factual showing at all of "probable cause" or reasonable justification for conduct of the investigation and intrusion by court process into the private files and records of the respondent;

(ii) "that an agency need not demonstrate facts showing the probability of coverage under the [pertinent regulatory] statute or the likelihood of violation of the statute to secure enforcement of a subpoena" (opinion p. 4011);

(iii) that the "probable cause" requirement of the Fourth Amendment is, in effect, abrogated or suspended or otherwise inapplicable to administrative subpoenas *duces tecum* seeking so-called "jurisdictional facts" with respect to possible statutory "coverage" or regulatory jurisdiction of the agency over the business of the respondent, with the result that the district court asked to issue a subpoena enforcement order may not require the agency to show any facts at all upon which issuance of the subpoena was based as a condition to issuance of the order; instead, that court must simply "rubber stamp" the agency's application as written,

without even the slightest showing having been made of any factual basis for the invasion by subpoena of the privacy of the respondent's business records, on the theory that it will be sufficient protection for the respondent's constitutional rights if, after his files have been produced for agency inspection at great cost and made a permanent part of the government's records, a "full hearing" *may* be provided for respondent's arguments (that there is no factual cause for the agency to investigate him and that it has no statutory authority to investigate or regulate the kind of business he does) at some possible future time *if and when* the agency decides to take some regulatory action against him;

(iv) that there is no conflict whatever between the holding by that court in *SEC v. Wall Street Transcript Corp.*, 422 F.2d 1371 (2d Cir. 1970), *cert. denied*, 398 U.S. 958 (1970), (that no showing of "probable cause" need be made under the Fourth Amendment for enforcement by the SEC through judicial process of a subpoena for business records seeking "jurisdictional facts") and that of the Supreme Court in *See v. Seattle*, 387 U.S. 541 (1967), (that the "probable cause" requirement of the Fourth Amendment is applicable to "administrative agencies at all levels of government," *i.e.*, both state and federal, and "to a broad range of investigations," including, "inspection of the structure in which a business is housed, as in this case, or inspection of business products, *or a perusal of financial books and records.*" [387 U.S. at 544, emphasis supplied]);

(v) that the holding of *See v. Seattle*, *supra*, is limited in its application to cases in which "there was governmental entry onto private property" and does not apply to cases involving "an administrative subpoena for the production of books and records, which has been termed a 'constructive' search" — despite plain language to the contrary (quoted above) by the Supreme Court in *See v. Seattle* itself;

(vi) that it was a reversible error of law and not a ruling within the discretion of the district court, for Judge Tenney

to rule that the court would first order production of facts relevant to the issue of "coverage" or regulatory jurisdiction by the SEC and suspend production of facts (banking records and relationships) not relevant to that issue, subject to a subsequent showing by the Commission that the respondent in fact sell "securities" and not "commodities" and therefore fall within the SEC's regulatory and investigative jurisdiction;

(vii) that there is no direct conflict between the holding of that court in *Newmark & Co. v. Wirtz*, 330 F.2d 576, 578 (2d Cir. 1964) (that the SEC may conduct, by district court subpoena enforcement order and *without any showing of factual "probable cause"* in so-called "initial determination of coverage" situations, "simultaneously . . . a full inquiry into both potential cover *and* potential [substantive] violations . . . in aid of such investigations the Commission may issue subpoenas which will produce information on both issues" [op., p. 4012]) and that of the Supreme Court three years later in *See v. Seattle*, 387 U.S. 541 (1967) (that the "probable cause" requirement *applies* in such subpoena situations with no exception indicated for "initial determination" cases);

(viii) that it was a reversible error of law and not a proper exercise of the jurisdiction and discretion of the district court for District Judge Tenney to require that the SEC make to every person from whom documents or testimony is requested pursuant to the court's order a statement in form prescribed by the court and quoted in the opinion of June 7 herein (p. 4014-4015), designed to soften or reduce the potential *in terrorem* effect of communications by a federal law enforcement agency with respondent's customers and salesmen and resulting damage to the vital business relationships between respondents, their salesmen, and their customers;

(ix) that Congress did not expressly deprive the SEC of authority to regulate or to investigate sales such as those made by the respondents involving non-negotiable documents

of title to specific, identified casks of Scotch whisky when, in 1934, the definition of "security" in Section 2(1) of the Securities Act was amended and the sale of "certificate[s] of interest in property, tangible or intangible" was removed from the regulatory jurisdiction of the Commission by the deletion of those words from the definition therein set forth; and

(x) that the term "investment contract" in Section 2(1) of the Securities Act, which has been given a broad and completely unspecific "remedial" construction in a number of *civil* injunction actions commenced by the SEC, but which is one element of the definition of a federal crime (selling securities to the public without federal registration or exemption from the registration requirement) and has *never* been given a narrow, specific definition which would enable a reasonable man to know what sales are criminal and which are not, is not "void for vagueness" under the holdings of such Supreme Court cases as *Connally v. General Construction Co.*, 269 U.S. 385 (1926), and *Lanzetta v. New Jersey*, 306 U.S. 451 (1939).

Petitioners respectfully submit that the court below was patently in error on every one of the 10 interrelated holdings or conclusions of law set forth above and that the constitutional issues involved in this appeal are of such exceptional importance and timeliness, and many conclusions reached by the court below in its opinion are so obviously subject to serious question as being in direct conflict with controlling Supreme Court decisions, that a writ of certiorari should be granted to review that decision.

Despite the conceded absence of any factual showing at all, however slight, of "probable cause" by the SEC to the district court in this case, the circuit court proceeded, in complete derogation of the Fourth Amendment, to require that the instant subpoenas be enforced in full as written by the SEC and without even the slightest modification by the

district court of the SEC's handiwork because (A) the SEC claims the instant subpoenas to have been issued in search of "jurisdictional facts" and (B) whenever such a self-serving statement is made by an SEC investigator, "the Commission must be free without undue interference or delay to conduct an investigation which will adequately develop a factual basis for a determination as to whether particular activities come within the Commission's regulatory authority" (opinion, p. 4007) and "the Commission . . . is entitled simultaneously to conduct a full inquiry into both potential coverage [jurisdiction to investigate] *and potential violations*" of the federal securities statutes — all without any showing of factual "probable cause" ever having been made by the investigating agents of the federal government to satisfy the "probable cause" requirement of the Fourth Amendment and to show that there was, in the first instance, some factual basis for invading the privacy of private records and not mere whim, or unfounded curiosity, or malice, or the desire to discredit a political opponent of the administration presently in power.

POINT II

The term "investment contract" contained in Section 2(1) of the Securities Act is void for vagueness under the due process clause of the Fifth Amendment.

Petitioners have made a substantial claim that their rights under the due process clause of the Fifth Amendment will be violated if the order below is enforced against them on the theory that the interests in specific, identified casks of Scotch whisky aging in storage in government supervised and bonded warehouses in Scotland which they offer and sell are, or "may be," "investment contracts" within the meaning of that term as used in Section 2(1) of the Securities Act, because that term fails to satisfy constitutional standards of specificity for criminal statutes set forth in the void-for-vagueness cases decided by the Supreme Court over

many years, including, *Connally v. General Construction Co.*, 269 U.S. 385 (1926), and *Lanzetta v. New Jersey*, 306 U.S. 451 (1939). And they argue that this court should hold that term void and unenforceable against them on vagueness grounds on this appeal.

Here we have a plain and clear-cut case of a term used to define an element of a federal crime which suffers not one, but two fatal "vagueness" defects: (i) it fails completely to provide to a man of reasonable intelligence, on the face of the statute as written, "fair warning" of what things he may safely sell for investment purposes without risking indictment under Section 5 of the Securities Act and what things he definitely can *not* sell without such risk and (ii) it delegates to the Commission and its staff discretion in defining conduct that will be deemed a crime and prosecuted or deemed a civil wrong and sued-upon for an injunction without providing any reasonably clear *objective* limitations upon the exercise of that delegated discretion. This case is a good example of abuse of that discretion and of the total absence of any meaningful objective guidelines for counsel or the court to look to in limiting it. The vagueness problem in this appeal with the term "investment contract" is a very serious, substantial and important one urged most vigorously by counsel for petitioners. That problem exists. It must be dealt with by this Court. It has extremely broad implications in terms of SEC regulatory activities all over the country. It simply will not do for the Commission to attempt to belittle that problem and sweep it under the rug by characterizing it as nonexistent or "without merit."

In the statutory combination of Sections 5 and 2(1) of the Securities Act, we have a rather unusual statutory animal. Under Section 5 it is a federal crime to sell to the public "securities" as defined in Section 2(1), absent an effective registration with the SEC. However, unlike most criminal statutes, these are used most frequently by the SEC as the basis for civil rather than criminal proceedings on the perfectly valid theory that violation of any criminal statute is

a civil wrong which a court of equity can and should enjoin. Consequently, *all of the cases cited by the court* in its opinion as interpreting Section 2(1) definitively *are civil, not criminal*, cases; and the broad, remedial reading given the definition in those cases is understandable in the civil enforcement context in which those decisions were rendered.

However, an anomalous jurisprudential situation is created by those broad and open-ended decisions when one considers that every SEC investigation, including the instant one, is potentially criminal in character in the absence of an express stipulation or waiver by the Commission to the contrary which is not present in this case.

If the remedies provided in Section 5 were exclusively civil and there was a separate criminal statute with a definition of "security" more narrowly defined than Section 2(1), petitioners would probably have no vagueness argument under the Fifth Amendment in this case. But that is not the situation we have.

What we have is a criminal statute that has been construed by the federal courts, including the Supreme Court, as if it provided for civil remedies only. The result is that language has been used in the opinions under Section 2(1) which is not appropriate for the strict and objectively clear standards that must be applied to criminal statutes, and that language has, in turn, led the Commission and its staff to interpret that section in a broad-gauge fashion which imposes no objective and reasonably discernible limitations upon either (i) the conduct made criminal by Section 5 or (ii) the discretion of the Commission to prosecute or take other legal action thereunder. Indeed, at page 32 of its main brief below, the Commission itself argued that "the word ['investment contract,' *sic.*] was deliberately left open-ended . . ." by Congress.

If that is so (and it is), then the term is *a fortiori* too vague to withstand vagueness scrutiny as a definition of a material element of a federal crime under the standards set forth in *Connally* and *Lanzetta, supra.*

CONCLUSION

For the reasons set forth above, it is respectfully submitted that this petition for a writ of certiorari to review the judgment and opinion of the Second Circuit should be granted.

Respectfully submitted,

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October 19, 1973

ORDER DENYING A REHEARING
(Filed July 25, 1973)

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

At a stated term of the United States Court of Appeals in and for the Second Circuit held at the United States Court House, in the City of New York on the twenty-fourth day of July one thousand nine hundred and seventy-three.

Docket Nos. 73-1395, 73-1444-5-6

Present:

HON. J. EDWARD LUMBARD,

HON. HENRY J. FRIENDLY,

Circuit Judges,

HON. ROSZEL C. THOMSEN,

District Judge.

In the Matter of an Application to
Enforce Administrative Subpoenas
Duces Tecum of the

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellant,

v.

BRIGADOON SCOTCH DISTRIBUTING COMPANY,
MILBANK TRADING CO. INC., and
LEITH-MOOR SCOTCH WHISKY CO.,

Defendants-Appellants.

Order Denying a Rehearing

A petition for a rehearing having been filed herein by counsel for the appellants,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is denied.

s/A. Daniel Fusaro
A. DANIEL FUSARO
Clerk

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

At a stated term of the United States Court of Appeals in and for the Second Circuit held at the United States Court House, in the City of New York on the twenty-fourth day of July one thousand nine hundred and seventy-three.

Docket Nos. 73-1395, 73-1444-5-6

In the Matter of an Application to
Enforce Administrative Subpoenas
Duces Tecum of the

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellant,

v.

BRIGADOON SCOTCH DISTRIBUTING COMPANY,
MILBANK TRADING CO. INC., and
LEITH-MOOR SCOTCH WHISKY CO.,

Defendants-Appellants.

Order Denying a Rehearing

A petition for a rehearing containing a suggestion that the action be reheard en banc having been filed herein by counsel for the appellants, and no active circuit judge having requested that a vote be taken on said suggestion.

Upon consideration thereof, it is

Ordered that said petition be and it hereby is denied.

s/A. Daniel Fusaro
A. DANIEL FUSARO
Clerk

OPINION OF THE COURT BELOW

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 832-35—September Term, 1972.

(Argued March 30, 1973 Decided June 7, 1973.)

Docket Nos. 73-1395
73-1444-46

SECURITIES AND EXCHANGE COMMISSION,

Petitioner-Appellee and Cross-Appellant,

—v—

BRIGADOON SCOTCH DISTRIBUTING CO., MILBANK TRADING CO., INC. and LEITH-MOOR SCOTCH WHISKY CO.,

Respondents-Appellants and Cross-Appellees.

Before:

LUMBARD and FRIENDLY, *Circuit Judges*, and THOMSEN, *District Judge*.*

Appeals from an order of the District Court for the Southern District of New York, Tenney, *J.*, granting enforcement in part and denying enforcement in part to subpoenas *duces tecum* issued by the Securities and Exchange Commission during an investigation to determine

* Of the District of Maryland, sitting by designation.

whether certain interests in whisky sold by appellants represent "securities" within the meaning of the federal securities laws and, if so, to determine whether any securities laws violations have occurred.

Affirmed in part and reversed in part.

WALTER P. NORTH, Acting General Counsel, Securities and Exchange Commission, Washington, D.C. (Michael A. Macchiaroli, Attorney, Securities and Exchange Commission, Washington, D.C. on the brief), *for Applicant-Appellee and Cross-Appellant.*

BRADLEY R. BREWER, Esq., New York, New York, *for Respondent-Appellant Brigadoon Scotch Distributing Co.*

ARTHUR J. HOMANS, Esq., New York, New York, *for Respondent-Appellant Milbank Trading Co., Inc.*

LUMBARD, *Circuit Judge:*

On January 26, 1972, the Securities and Exchange Commission ("SEC") applied to the district court for the Southern District of New York for an order pursuant to section 22(b) of the Securities Act of 1933, 15 U.S.C. § 77v (b), and section 21(c) of the Securities Exchange Act of 1934, 15 U.S.C. § 78u(c), directing compliance with subpoenas *duces tecum* issued to Brigadoon Scotch Distributing Co. ("Brigadoon"), Milbank Trading Co., Inc. ("Milbank"), and Leith-Moor Scotch Whisky Co. ("Leith-Moor"). The district court in two memorandum decisions and an order, which was entered on February 14, 1973, granted enforcement of the subpoenas in part and denied enforce-

ment in part. Brigadoon, Milbank, Leith-Moor and the Commission have each appealed.

On March 13, 1973, a panel of this court ordered these appeals consolidated, granted a stay of the district court's Order, and ordered the appeals to be heard on an expedited basis. For the reasons stated below, we affirm so much of the district court order as enforces the Commission's subpoenas, and reverse so much of the order as denies enforcement of the subpoenas.

I

Under section 20(a) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. § 77t(a), and section 21(a) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78u(a), the SEC is empowered to conduct investigations into possible violations of the federal securities laws. Pursuant to these provisions the Commission on February 4, 1971 issued an "Order Directing Private Investigation and Designating Officers to Take Testimony (the "Order").[1] The Order provided for the investigation

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1 The Order contains the following statement of the underlying basis for its issuance:

> Members of its staff have reported information to the Commission which tends to show that:
>
> A. During the period from approximately January 1, 1969 to the present, Brigadoon, Highland, Edinburgh and Milbank, their officers, directors, employees, representatives, franchisees and others while engaged in the business of a broker-dealer in securities have been and are offering to sell, selling and delivering after sale to members of the public certain securities namely whisky warehouse receipts.
>
> B. While engaged in the offer and sale of such securities, such persons made to purchasers and prospective purchasers untrue statements of material facts and omitted to state material facts necessary to make the statements made, in the light of the circumstances under which they were made, not misleading, concerning, among other things:

of certain named persons, together with Brigadoon and Milbank, or "any other persons," to ascertain whether they had engaged or were about to engage in any acts or practices in connection with the offer and sale of whisky warehouse receipts in violation of sections 5(a), 5(c) and 17(a) of the Securities Act, 15 U.S.C. §§ 77e(a), 77e(c), & 77q(a), and sections 10(b) and 15(a) of the Exchange Act, 15 U.S.C. §§ 78j(b) & 78*o*(a), and Rule 10b-5, 17 C.F.R. § 240.10b-5 thereunder. The Order also provided, in accordance with section 19(b) of the Securities Act, 15 U.S.C. §77s(b), and section 21(b) of the Exchange Act, 15 U.S.C. § 78u(b), for the appointment of several members of the Commission staff as officers of the Commission with the power, among other things, to subpoena witnesses and require the production of any books, papers, correspondence, memoranda or other records deemed relevant and material to the investigation.

On April 14, 1971, pursuant to the Commission's Order a subpoena *duces tecum* was issued to Brigadoon Scotch Distributors, Ltd.,[2] which required Brigadoon to produce at the Commission's New York Regional Office the following eight categories of documents:

> "1. A list of all persons with their addresses who have purchased whisky warehouse receipts or whisky from Brigadoon Scotch Distributors, Ltd. or with the aid of Brigadoon Scotch Distributors, Ltd.

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(1) The availability of a competitive public market for the purchase and sale of such securities;

(2) The commission or mark-up taken by the sellers of such securities;

(3) The background of persons selling such securities;

(4) The profitability of investments in such securities; and

(5) The risks of investment in such securities.

2 The Commission's subpoena mistakenly refers to Brigadoon Scotch Distributing Co. as Brigadoon Scotch Distributors, Ltd.

2. A list of all persons with their addresses who have been employed by Brigadoon Scotch Distributors, Ltd. on either a salary or commission basis for the purpose of selling whisky warehouse receipts or whisky.

3. Copies of all literature sent by Brigadoon Scotch Distributors, Ltd. or its agents to prospective purchasers of whisky warehouse receipts or whisky.

4. Copies of all advertisements placed in the news media by Brigadoon Scotch Distributors, Ltd. or its agents in connection with the sale of whisky warehouse receipts or whisky.

5. A list of all parents, subsidiaries or affiliates of Brigadoon Scotch Distributors, Ltd.

6. A list of all persons with their addresses who are or have ever been officers, directors, partners or shareholders of Brigadoon Scotch Distributors, Ltd.

7. Copies of any financial statements, income statements or balance sheets reflecting Brigadoon Scotch Distributors, Ltd.'s financial condition for any period from January 1, 1968.

8. A list of all banks, factors, lending institutions or other corporations or persons which Brigadoon Scotch Distributors, Ltd. has used from January 1, 1968 to date in connection with the financing of the business of buying or selling whisky warehouse receipts or whisky, including but not limited to, places where funds have been deposited, loans obtained and transfer facilities used."

On April 14, 1971, a virtually identical subpoena was issued to Milbank Trading Company, Inc.; and on July 9,

1971, a subpoena, similar in all respects but one, was sent to Leith-Moor Scotch Whisky Co. The single difference in the Leith-Moor subpoena consisted of the omission of a request for the information contained in item (7) of the Brigadoon and Milbank subpoenas. Thus item (7) of the Leith-Moor subpoena corresponded to item (8) of the Brigadoon and Milbank subpoenas. The three companies responded with varying amounts of information, but none complied fully with the subpoenas. As a result, the Commission commenced these proceedings to compel compliance.

Judge Tenney, relying on our decision in *SEC* v. *Wall Street Transcript Corp.*, 422 F.2d 1371 (2d Cir.), cert. denied, 398 U.S. 958 (1970), held in a memorandum decision dated September 5, 1972, that the information called for in items (1) through (6) of the three subpoenas should be produced. As to items (7) and (8) of the Brigadoon and Milbank subpoenas and item (7) of the Leith-Moor subpoena, Judge Tenney found that the information required would be irrelevant unless the Commission could demonstrate that respondents below were selling securities. To avoid "an unnecessary imposition on Respondents" that "possibly would damage their business" he denied enforcement of this portion of the subpoenas with leave to the SEC to renew its application upon a showing that the documents involved were in fact securities subject to regulation by the Commission. In addition, to lessen the impact on respondents' business which might result from inquiries by the Commission directed to respondents' customers and employees based upon the information supplied in items (1) and (2) of the subpoenas, Judge Tenney also provided that appropriate protective provisions should be entered in the final order.

Motions to reargue were made by the three respondents below and the SEC. Judge Tenney, in a memorandum de-

cision dated January 10, 1973, granted the motions and adhered to his prior decision. The final Order, of February 14, 1973, required *inter alia,* that the Commission "recite to each and every business entity and person from whom documents, information, or testimony is requested" a statement to the effect that the SEC is conducting an investigation under the "authority and supervision" of the district court to determine whether the interests in whisky sold by appellants are securities; that the Commission has made no determination yet as to coverage under the federal securities laws; that no charges are pending; and that appellants contend that they sell "commodities" not subject to SEC regulation.

On this appeal Brigadoon, Milbank, and Leith-Moor assert that the district court relied improperly on the *Wall Street Transcript* case, *supra,* and that they should not be forced to produce the information called for in items (1) through (6) of the subpoenas. The SEC contends that, to the contrary, the subpoenas should have been enforced in their entirety, including items (7) and (8) of the Brigadoon and Milbank subpoenas and item (7) of the Leith-Moor subpoena, and that the Commission's investigators should not be required to recite the information contained in the protective provisions contained in the order entered below. We will consider each of these contentions.

II

Brigadoon, Milbank, and Leith-Moor have maintained throughout these proceedings that what they sell are documents of title to specific casks of scotch whisky aging in government bonded warehouses in Scotland, and not whisky warehouse receipts, as the Commission apparently main-

tains.[3] These appellants[4] contend that the SEC has no regulatory power over them because Congress in amending the Securities Act in 1934 to eliminate the phrase "certificate[s] of interest in property, tangible or intangible" from the definition of a "security" contained in section 2(1) of the Securities Act, 15 U.S.C. § 77b(1), intended to eliminate from coverage under the federal securities laws documents of title such as they sell. According to appellants the current definition of a security, which includes the term "investment contract," cannot possibly be construed to cover either negotiable warehouse receipts (which they claim they do not sell) or non-negotiable documents of title (which they claim they do sell). Appellants argue, therefore, that before the Commission can subpoena information from them, the Commission must demonstrate that there is "reasonable, factual cause for a belief that the sales made by these three [appellants] may constitute the sale of 'securities' or 'investment contracts' within the meaning of Section 2(1) of the Securities Act."[5] In particular, they urge that the district court must make some initial determination as to statutory coverage and that

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3 It seems that at least up until July 6, 1967, the SEC took the position that certain ownership interests in *whisky* similar to those that respondents allege that they sell were not securities. See letter dated July 6, 1967, from Arthur F. Mathews, Chief, Branch of Criminal Reference and Special Proceedings, Division of Trading and Markets, SEC (by Peter J. Adolph, attorney) to Allen E. Bachman, Executive Vice-President, National Better Business Bureau, Inc. On the other hand, Securities Act Release No. 5018 (Nov. 4, 1969) indicates that it is also the Securities and Exchange Commission's position that *whisky warehouse receipts* may indeed be securities within the meaning of the federal securities laws.

4 Although Brigadoon, Milbank and Leith-Moor are not only appellants in this action but also cross-appellees, for the sake of clarity they will be referred to solely as "appellants," while the Securities and Exchange Commission will be referred to by name as the SEC or the Commission.

5 Joint brief of respondents-appellants at 51.

the fourth amendment's "probable cause" requirement demands that the Commission show enough facts to demonstrate that "reasonable grounds" exist for issuing subpoenas to appellants and compelling the production of documents.[6]

Appellants raise serious questions about whether their activities are subject to regulation by the SEC. Should the Commission seek to exercise regulatory control over appellants' business affairs at some future date, whether by means of a section 5 injunctive suit or otherwise, appellants will be entitled to a full hearing on their contentions. However, it has long been settled that such issues are not to be decided in subpoena enforcement actions. The Commission must be free without undue interference or delay to conduct an investigation which will adequately develop a factual basis for a determination as to whether particular activities come within the Commission's regulatory authority.

In 1946 in *Oklahoma Press Pub. Co.* v. *Walling*, 327 U.S. 186 (1946), a case involving the administration of the Fair Labor Standards Act, 52 Stat. 1060, the Supreme Court stated what has since become the rule for interpreting regulatory statutes; namely, that it is for the agency rather than the district courts to determine in the first instance the question of coverage in the course of the preliminary investigation into possible violations. 327 U.S. at 214. See *Endicott Johnson Corp.* v. *Perkins*, 317 U.S. 501 (1943). As to what showing of coverage, if any, an

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6 Appellants also argue that the term "investment contract" contained in section 2(1) of the Securities Act, 15 U.S.C. § 77b(1), is void for vagueness. See *Connally* v. *General Const. Co.*, 269 U.S. 385, 391 (1926). In light of the many Supreme Court decisions defining and applying the term, *e.g.*, *S.E.C.* v. *C.M. Joiner Leasing Corp.*, 320 U.S. 344 (1943); *S.E.C.* v. *W.J. Howey Co.*, 328 U.S. 293 (1946); *S.E.C.* v. *United Benefit Life Ins. Co.*, 387 U.S. 202 (1967), we find such a position to be untenable.

agency must make to secure judicial enforcement of a subpoena in light of the fourth amendment, the Court in *Oklahoma Press* stated that "any possible constitutional requirement of that sort was satisfied by the Administrator's showing in this case, including not only the allegations concerning coverage, but also that he was proceeding with his investigation in accordance with the mandate of Congress and that the records sought were relevant to that purpose." 327 U.S. at 215-16. The Court said of the requirement of "probable cause" as applied to subpoena enforcement actions:

> The requirement of "probable cause, supported by oath or affirmation," literally applicable in the case of a warrant, is satisfied in that of an order for production by the court's determination that the investigation is authorized by Congress, is for a purpose Congress can order, and the documents sought are relevant to the inquiry. 327 U.S. at 209.

Subsequently, the Supreme Court on several occasions has reaffirmed the doctrine enunciated in *Oklahoma Press*. See *United States* v. *Morton Salt Co.*, 338 U.S. 632 (1950); *F.T.C.* v. *Crafts*, 355 U.S. 9 (1957); *United States* v. *Powell*, 379 U.S. 48 (1964). In *United States* v. *Morton Salt Co., supra*, the Court indicated that even if the agency request is motivated by "nothing more than official curiosity," the subpoena is enforceable because agencies have a legitimate interest in seeing that the law and the public interest are maintained—assuming, of course, that the agency is acting within its authority and the information requested is relevant to the inquiry. 338 U.S. at 652.

Summarizing this area of the law, this court stated in 1970 in *SEC* v. *Wall Street Transcript Corp.*, 422 F.2d 1371, 1375 (2d Cir.), cert. denied, 398 U.S. 958 (1970), which was relied on by the district court:

> [I]t has long been established that the question of the inclusion of a particular person or entity within the coverage of a regulatory statute is generally for initial determination by an agency, subject to review on direct appeal, rather than for a district court whose jurisdiction is invoked to enforce an administrative subpoena. So long as an agency establishes that an investigation "will be conducted pursuant to a legitimate purpose, that the inquiry may be relevant to the purpose, that the information sought is not already within [its] possession, and that the administrative steps required * * * have been followed," no showing of probable cause need be made to the district court unless a statute indicates otherwise. United States v. Powell, 379 U.S. 48, 57-58, 85 S.Ct. 248, 255, 13 L.Ed. 2d 112 (1964); FTC v. Crafts, 355 U.S. 9, 78 S.Ct. 33, 2 L.Ed2d 23 (1957); Oklahoma Press Pub. Co. v. Walling, 327 U.S. 186, 66 S.Ct. 494, 90 L.Ed. 614, 166 A.L.R. 531 (1946); Endicott Johnson Corp. v. Perkins, 317 U.S. 501, 63 S.Ct. 339, 87 L.Ed. 424 (1948); 1 Davis, Administrative Law, § 3.12 (1958).

It is apparent from the SEC's Order in this case that its investigation has the legitimate purpose of determining whether the whisky or warehouse receipts sold by appellants, in the context of the representations or understandings that may surround their sale, are securities covered by the securities acts, and, if so, of determining whether any securities violations have occurred. The Securities Act and the Exchange Act, as indicated above, clearly authorize such investigations, *cf. Oklahoma Press Pub. Co., supra,* at 210 n. 47, and the information sought through the subpoenas is obviously relevant to the inquiry. There has been no suggestion that the SEC already has the information; nor have appellants raised

any substantial claim that the SEC has failed to follow the appropriate administrative steps set out in the statute.[7]

However, appellants argue that the decision of the Supreme Court in *See* v. *Seattle*, 387 U.S. 541 (1967), a case decided three years prior to *Wall Street Transcript, supra*, requires a factual showing by an agency of "reasonable grounds" to issue subpoenas, not merely a demonstration that the inquiry is legitimate under the governing statute and that the documents requested are relevant to the inquiry. We do not agree. In *See* v. *Seattle, supra*, the Court did nothing to change the well-established principles associated with the judicial enforcement of agency subpoenas. The owner of a commercial warehouse was seeking reversal of his conviction for refusing "to permit a representative of the City of Seattle Fire Department to

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7 Appellants do assert that the subpoenas issued to them do not stay within the investigative limits set out in the SEC's order. The order calls for the investigation of the offer and sale of whisky warehouse receipts; the subpoenas ask for information in connection with appellants' sales of "whisky warehouse receipts or *whisky*" (emphasis added). Although it is true that the investigative order does not use the term "whiskey," any claim that the staff exceeded its authority in issuing the subpoenas cannot withstand analysis. The order itself specifically names appellants Brigadoon and Milbank and authorizes an inquiry into whether they have been selling securities, namely whisky warehouse receipts, in violation of the securities laws. Appellants have taken the position that they sell titles to specific, identifiable casks of scotch whisky which are neither whisky warehouse receipts nor securities. Nevertheless, since appellants do not contend that they sell more than one type of ownership interest in whisky, it is perfectly apparent that the current investigation, including the three subpoenas at issue here, concerns the same activities specified in the Commission's order. A minor difference in nomenclature will not suffice to place the actions of the staff beyond its investigative authority.

What appellants would have us decide, under the guise of determining whether the subpoenas were within the authority conferred by the Commission on the staff, is whether respondents sell whisky or whisky warehouse receipts. As stated above, that determination, which concerns the critical issue of whether respondents' activities come within the coverage of the securities laws, is one that must be made initially by the SEC, not the court.

enter and inspect [his warehouse] without a warrant and without probable cause to believe that a violation of any municipal ordinance existed therein." 387 U.S. at 541. The Court reversed, holding that the fourth amendment requires an administrative agency to obtain a warrant before searching commercial premises.

In *See*, there was governmental entry onto private property, action that is markedly different from issuing an administrative subpoena for the production of books and records, which has been termed a "constructive" search, *Oklahoma Press Pub. Co., supra,* at 202, and which certainly involves a minimal invasion of privacy. Nevertheless, in *See* the Court referred approvingly to the standards associated with the judicial enforcement of administrative subpoenas as evidence that a warrant requirement would impose only a "necessary and a tolerable limitation on the right to enter upon and inspect commercial premises." 387 U.S. at 544. In a footnote the Court cited several cases, including *Oklahoma Press Pub. Co.* v. *Walling, supra,* and *United States* v. *Morton Salt Co., supra,* which stand for the proposition that for purposes of the fourth amendment's probable cause requirement it is sufficient if an agency shows that an investigation is within its authority and the materials requested are reasonably relevant. Thus, it is apparent that in *See* v. *Seattle, supra,* the Court in no way modified its previous holdings that an agency need not demonstrate facts showing either the probability of coverage under the statute or the likelihood of violation of the statute to secure enforcement of a subpoena.

Accordingly, we affirm that portion of the district court's order which requires appellants to produce items (1) through (6) listed in the subpoenas.

III

The SEC contends that it is also entitled to have the remainder of its subpoenas (items (7) and (8) of the Brigadoon and Milbank subpoenas and item (7) of Leith-Moor subpoenas) enforced on the same showing that the information requested is relevant to a legitimate aim of the investigation. We agree. Absent evidence of abuse by the Commission, *United States* v. *Powell*, 379 U.S. 48 (1964), it is entitled simultaneously to conduct a full inquiry into both potential coverage and potential violations. In aid of such investigation the Commission may issue subpoenas which will produce information on both issues. As we said in *Newmark & Co.* v. *Wirtz*, 330 F.2d 576, 578 (2d Cir. 1964):

> Although it might well save time and expense for all concerned if the Administrator first examined such records as were relevant to coverage and then proceeded beyond that only if convinced that appellant were covered, the Oklahoma Press decision makes it plain that the course of the investigation is for the Administrator to determine. If appellant believes that the nature of its operations is not such as to render it subject to the Act, it can properly litigate that issue if and when the Administrator attempts to enforce the Act's substantive requirements against it after the completion of the administrative investigation.

That the materials requested in items (7) and (8) of the Brigadoon and Milbank subpoenas are relevant to the issue of possible violations of the securities laws is indisputable. Copies of the companies' financial statements and a list of financial institutions involved in the "financing of the business of buying and selling whisky warehouse receipts or

whisky" will assist the Commission in determining, for example, whether appellants have violated either the financial responsibility[8] or anti-fraud[9] provisions of the federal securities laws. Barring other compelling considerations, then, these portions of the subpoenas must also be enforced.

The district court did suggest in support of its denial of enforcement of items (7) and (8) of the Brigadoon and Milbank subpoenas and item (7) of the Leith-Moor subpoena that production of the material requested "possibly would damage" appellants' business. It is unclear from the memorandum decisions of the district court to what extent it relied on this factor in refusing to order production of the requested materials. However, since appellants have been unable to show specifically how production of this information will result in harm to their business, it is apparent that the district court's refusal to enforce these items cannot be upheld on this ground alone.

It is true that while the SEC is entitled to great freedom in conducting its investigations, it is not at liberty to act unreasonably, and in appropriate circumstances the court may inquire into the reasons for an investigation and into its effects. For example, if a subpoena were not issued in good faith but to harass or pressure the subject of an investigation, or for any other improper purpose, then the court would be bound not to enforce the subpoena as issued. *United States* v. *Powell*, 379 U.S. 48, 58 (1964). Likewise, if it could be demonstrated that compliance with an agency

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8 Section 15(c)(3) of the Securities Exchange Act, 15 U.S.C. § 78o (c)(3), and Rules 15c3-1 through 15c3-3 thereunder, 17 CFR 240.15c3-1 through 15c3-3.

9 Section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a), and sections 10(b) and 15(c)(1) and (2) of the Securities Exchange Act, 15 U.S.C. §§ 78j(b), 78o(c)(1) & (2), and Rules 10b-5 and 15c1-1 through 15c2-11 thereunder, 17 CFR 240.10b-5 and 240.15c1-1 through 240.15c2-11.

subpoena would be *unnecessarily* burdensome, some limitation of the materials required would be warranted. But the burden of showing that an agency subpoena is unreasonable remains with the respondent, see *United States* v. *Powell, supra*, at 58; *United States* v. *Donaldson*, 400 U.S. 517, 527 (1971), and where, as here, the agency inquiry is authorized by law and the materials sought are relevant to the inquiry, that burden is not easily met. *Cf. Adams* v. *F.T.C.*, 296 F.2d 861 (8th Cir. 1961), cert. denied, 369 U.S. 864 (1962). Thus the mere suggestion by appellants of possible damage to their business activities is not sufficient to block an authorized inquiry into relevant matters. See *Newmark & Co.* v. *Wirtz*, 330 F.2d 576, 578 (2d Cir. 1964).

The Commission in its cross-appeal also asks that the order of the district court be modified by striking therefrom any requirement that there be given to every person from whom documents or testimony is requested the following statement:

> "An inquiry is being conducted by the Securities and Exchange Commission relative to the offer and sale of Scotch whisky and/or whisky warehouse receipts as an investment for the purpose of determining whether or not the interests in whisky being sold are 'securities' subject to regulation by the SEC. This proceeding is only an inquiry and is being conducted under the authority and supervision of a Federal District Court. No charge of violation of the federal securities laws has been made against the party concerning whom documents or information is being requested. The SEC has made no determination as to whether such interests in whisky are, or are not, 'securities'; such determination will ultimately be made by the Court. [Name of appropriate Respondent] contends that the whisky in-

terests which it sells are 'commodities' and are not 'securities' subject to regulation by the Commission".

We see no good reason to encumber the early stages of the Commission's investigation with a requirement that each person from whom information is sought be advised of the nature and status of the inquiry and the contentions of the parties. To do so would be merely to invite controversy and litigation over the contents of the statement to be given. Furthermore, where an agency investigation is rapidly developing and changing, it would be difficult, if not impossible, accurately and completely to summarize the current status of the proceedings. Every person doing business and every investor knows that government agencies conduct investigations for a variety of reasons, and most of them feel the duty to respond to a proper inquiry. As for those whose practices are investigated, it is a necessary hazard of doing business to be the subject of inquiry by a government regulatory agency. Thus, we see no sound basis for imposing on the Commission the requirement of reciting such a statement.[10]

Accordingly, we affirm so much of the district court's order as granted enforcement of items (1) through (6) of the Brigadoon, Milbank, and Leith-Moor subpoenas.

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10 In addition, it must be noted that the protective provisions inserted by the district court in this case are in certain respects inaccurate and incomplete. For instance, the first sentence states that the investigation is being conducted to determine if the interests in whisky that are being sold are 'securities' subject to SEC regulation. In fact, as has already been noted, the investigation is for a dual purpose: first, to determine if securities are involved and, second, to ferret out possible federal securities law violations. The following sentence further compounds the misleading quality of the notice by stating that the investigation "is being conducted under the authority and supervision of the Federal District Court." Actually, the investigation is completely under the supervision and control of the SEC and the district court's role is limited to enforcing subpoenas issued during the course of the inquiry.

We reverse the order of the district court insofar as it denies enforcement to items (7) and (8) of the Brigadoon and Milbank subpoenas and item (7) of the Leith-Moor subpoena, and imposes a requirement that the Commission supply certain specified cautionary material to those subpoenaed.

OPINION OF THE DISTRICT COURT (TENNEY, DISTRICT JUDGE)

(Filed September 6, 1972)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

In the Matter of an Application to
Enforce Administrative Subpoenas
Duces Tecum of the
SECURITIES AND EXCHANGE COMMISSION,

Applicant,

-against-

BRIGADOON SCOTCH DISTRIBUTING CO., MILBANK TRADING CO., INC., LEITH-MOOR SCOTCH WHISKY CO.,

Respondents.

TENNEY, J.

Applicant, Securities and Exchange Commission (the "Commission") applies to this Court for an order requiring respondent Brigadoon Scotch Distributing Co. ("Brigadoon"), Milbank Trading Co., Inc. ("Milbank") and Leith-Moor Scotch Whisky Co. ("Leith-Moor") to produce the documentary information required by subpoenas *duces tecum* issued by Applicant's staff and served upon Respondents.

The Court has jurisdiction to determine this action pursuant to Section 22(b) of the Securities Act of 1933 ("Securities Act") (15 U.S.C. Section 77v(b)) and Section 21(c) of the Securities Exchange Act of 1934 ("Exchange Act") (15 U.S.C. Section 78u(c)).

Opinion of the District Court

On February 4, 1971, the Commission issued an Order Directing Private Investigation and Designating Officers to Take Testimony (the "Order"). Pursuant to Section 20(a) of the Securities Act (15 U.S.C. Section 77t(a)) and Section 21(a) of the Exchange Act (15 U.S.C. Section 78u(a)), the Order directed the staff of the Commission to conduct a private investigation to determine whether or not certain named persons or others have engaged or are about to engage in acts or practices in connection with the purchase and sale of whiskey warehouse receipts in violation of Sections 5(a), 5(c) and 17(a) of the Securities Act (15 U.S.C. Sections 77e(a), 77e(c) and 77q(a)) and Sections 10(b) and 15(a) of the Exchange Act (15 U.S.C. Sections 78j(b) and 78o(a)) and Rule 10b-5 (17 C.F.R. Section 240.10b-5) thereunder.

Pursuant to Section 19(b) of the Securities Act (15 U.S.C. Section 77s(b)) and Section 21(b) of the Exchange Act (15 U.S.C. Section 78u(b)), and for the purposes of the directed investigation, the Order designated David M. Greenberg and other employees of the Commission as officers of the Commission and empowered them to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence and require the production of any books, papers, correspondence, memoranda or other records deemed relevant and material to the directed investigation.

Acting pursuant to the Order, Greenberg issued on April 14, 1971, a subpoena *duces tecum* to Brigadoon which called for Brigadoon to produce certain books, records and other written documents on April 27, 1971, at the Commission's New York Regional Office. The subpoena was served by certified mail pursuant to Rule 14(b)(3) (17 C.F.R. Section 201.14(b)(3)) of the Commission's Rules of Practice and Rule 8 (17 C.F.R. Section 203.8) of the Commission's Rules Relating to Investigations, and was received by Brigadoon on April 19, 1971.

On April 14, 1971, Greenberg also issued a subpoena *duces tecum* to Milbank. The subpoena called for Milbank to produce certain books, records and other written documents on April 27, 1971, at the Commission's New York Regional Office, was served by certified mail, and was received by Milbank.

On July 9, 1971, Greenberg issued a subpoena *duces tecum* to Leith-Moor which called for Leith-Moor to produce certain books, records and other written documents on July 21, 1971, at the Commission's New York Regional Office, was served by certified mail, and was received by Leith-Moor on July 12, 1971.

The subpoenas require production of the following:

> (1) a list of all persons with their addresses who have purchased whiskey warehouse receipts or whiskey from or with the aid of the Respondents (as to Leith-Moor, this requirement was limited to the period from February 1, 1971, to date);
>
> (2) a list of all persons with their addresses who have been employed by the Respondents for the purpose of selling whiskey warehouse receipts or whiskey;
>
> (3) copies of all literature sent by the Respondents to prospective purchasers of whiskey warehouse receipts or whiskey;
>
> (4) copies of all advertisements placed in the news media by the Respondents or their agents in connection with the sale of whiskey warehouse receipts or whiskey;
>
> (5) a list of all parents, subsidiaries or affiliates of the Respondents;

(6) a list of all persons with their addresses who are or who have ever been officers, directors, partners or shareholders of the Respondents;

(7) as to Brigadoon and Milbank only, copies of any financial statements, income statements or balance sheets reflecting these Respondents' financial condition from January 1, 1968, to date; and

(8) a list of all banks, factors, lending institutions or other corporations or persons which Respondents have used in connection with the financing of their business of buying and selling whiskey warehouse receipts or whiskey, including but not limited to places where funds have been deposited, loans obtained and transfer facilities used. This requirement was limited as to Brigadoon and Milbank to the period from January 1, 1968, to date and as to Leith-Moor to the period from January 1, 1971, to date. (This item is listed as item 7 on the Leith-Moor subpoena.)

Respondents strongly contend that they are not doing business with "whiskey warehouse receipts" and have submitted evidence in support of such contention. However, little purpose would be served in a discussion of such contentions much as the Court might be inclined to give weight to them.*

> "[I]t has long been established that the question of the inclusion of a particular person or entity within the coverage of a regulatory statute is generally for initial determination by an agency, subject to review on direct appeal, rather than for a district court whose jurisdiction is invoked to enforce an

* The present methods used by Respondents would appear to be distinguishable from those employed in the past. *See e.g. Penfield Co. v. SEC*, 143 F.2d 746 (9th Cir.), *cert. denied*, 323 U.S. 768 (1944); *SEC v. Bourbon Sales Corp.*, 47 F. Supp. 70 (W.D. Ky. 1942).

> administrative subpoena. So long as an agency establishes that an investigation will be conducted pursuant to a legitimate purpose, that the inquiry may be relevant to the purpose, that the information sought is not already within [its] possession, and that the administrative steps required . . . have been followed, 'no showing of probable cause need be made to the district court unless a statute indicates otherwise. United States v. Powell, 379 U.S. 48, 57-58, 85 S.Ct. 248, 255, 13 L.Ed.2d 112 (1964); FTC v. Crafts, 355 U.S. 9, 78 S.Ct. 33, 2 L.Ed.2d 23 (1957); Oklahoma Press Pub. Co. v. Walling, 327 U.S. 186, 66 S.Ct. 494, 90 L.Ed. 614, 166 A.L.R. 531 (1946); Endicott Johnson Corp. v. Perkins, 317 U.S. 501, 63 S.Ct. 339, 87 L.Ed. 424 (1943); 1 Davis, Administrative Law, Section 3.12 (1958). If these criteria are satisfied, the court will order enforcement unless there is danger that its process may be abused. United States v. Powell, 379 U.S. at 58, 85 S.Ct. 248." *SEC v. Wall Street Transcript Corp.*, 422 F.2d 1371, 1375 (2d Cir.), *cert. denied*, 398 U.S. 958 (1970). *See also Newmark & Co. v. Wirtz*, 330 F.2d 576 (2d Cir. 1964).

Furthermore, since there is no dispute that Respondents in the conduct of this particular business make use of the mails,

> "the authority to issue the subpoena is controlled by the express terms of the particular statute involved. In this case Section 19(b) of the Act [15 U.S.C. Section 77s(b)] provides: 'For the purpose of all investigations which, in the opinion of the Commission, are necessary and proper for the enforcement of this subchapter the Commission may 'require the production of any books, papers, or other documents which the Commission deems relevant or material to the inquiry.' Unless the action

> of the Commission in undertaking this investigation is arbitrary and unreasonable or without any evidence to support the charges made against the respondent, its action in so doing should not be reviewed by the Court in this proceeding." *SEC v. Bourbon Sales Corp.*, 47 F. Supp. 70, 72 (W.D. Ky. 1942).

There would seem to be no question that the inquiry is relevant to the purpose, that the information sought is not already in the Commission's possession, and that the required administrative steps have been followed. Respondents' principal objections to the subpoenas are directed primarily against items 1, 2, 7 and 8, which are listed *supra*.

The material sought by items 1 and 2 is clearly relevant to the inquiry. The critical factor which the Commission must consider in assessing the existence or non-existence of a "security" is the extent to which investors rely on the services of others in realizing a profit on their money. In such a case the Commission may have to seek proof "outside the instrument itself". *SEC v. C. M. Joiner Leasing Corp.*, 320 U.S. 344, 355 (1943). Therefore, the Commission must review Respondents' sales literature and advertisements and speak with a selection of Respondents' salesmen, officers and purchasers (or investors, as the case may be) to determine whether there were oral representations in addition or contrary to the written representations.

Although Respondents assert that complying with items 1 and 2 will be damaging to their business, such damage, if any, may be lessened by appropriate protective provisions in an order to be entered herein along the lines suggested by Respondent Leith-Moor in its Memorandum of Law or by direct communication by Respondents with the persons involved in these items.

With respect to item 8 (item 7 of the Leith-Moor subpoena), the inquiry sought would appear to be relevant if indeed "securities" are involved herein. Absent such a

showing, such inquiry would not appear to be relevant on the part of the Commission. If the transactions in question do involve "securities" this can be developed or disproved through the inquiry sought under items 1 and 2, and until this is done inquiry under item 8 would appear an unnecessary imposition on Respondents and possibly would damage their business.

Accordingly, the order to be entered herein enforcing the subpoenas will direct compliance with all items other than items 7 and 8 of the Brigadoon and Milbank subpoenas and item 7 of the Leith-Moor subpoena with leave to renew the application for enforcement as to these items on a showing that the documents involved herein in the light of the circumstances under which they are issued do in fact constitute securities subject to regulation by the Commission.

Submit order in conformity herewith on five days' notice.

Dated: New York, New York
September 5, 1972

CHARLES H. TENNEY
U.S.D.J.

OPINION OF THE DISTRICT COURT (TENNEY, DISTRICT JUDGE) ON REARGUMENT

(Filed January 10, 1973)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

In the Matter of an Application to
Enforce Administrative Subpoenas
Duces Tecum of the
SECURITIES AND EXCHANGE COMMISSION,

Applicant,

-against-

BRIGADOON SCOTCH DISTRIBUTING CO.,
MILBANK TRADING CO., INC.,
LEITH-MOOR SCOTCH WHISKY CO.,

Respondents.

TENNEY, J.

This is a motion to reargue applicant's motion to enforce certain administrative subpoenas *duces tecum* of applicant, which application was granted in part and "denied" in part by this Court in its decision of September 5, 1972, on the grounds that the Court "overlooked certain matters and controlling decisions." Respondents Brigadoon and Leith-Moor in turn request that the Court reconsider and modify its prior decision even to the extent of denying enforcement *in toto* against them of the subpoenas.

While the Court is reluctant to grant the motions for reargument, it has heard the parties and finds that some clarification is in order. Insofar as the question of the inclusion of respondents or their activities within the coverage of the Securities Act of 1933 or the Securities Exchange Act of 1934 is concerned, the Court has recognized

that this is a matter "generally for initial determination by an agency, subject to review on direct appeal, rather than for a district court whose jurisdiction is invoked to enforce an administrative subpoena" and without any showing of probable cause. *SEC v. Wall Street Transcript Corp.*, 422 F.2d 1371, 1375 (2d Cir.), *cert. denied*, 398 U.S. 958 (1970). Accordingly, the Court already has granted enforcement of all of the items except items 7 and 8 of the Brigadoon and Milbank subpoenas and item 7 of the Leith-Moor subpoena "with leave to renew the application for enforcement as to these items on a showing that the documents involved herein [*i.e.*, whiskey warehouse receipts] in the light of the circumstances under which they are issued do in fact constitute securities subject to regulation by the Commission." (Memorandum Opinion of September 5, 1972, at 8.) The reason for this "postponement" in the enforcement of two items in the subpoenas was not due to the Court's having overlooked "controlling decisions" but on its having examined them more closely than did applicant, and further upon its conception of the Court as one of equity and not as a "rubber-stamp" for agency action. *Shasta Minerals & Chemical Co. v. SEC*, 328 F.2d 285 (10th Cir. 1964).

As recently as July 6, 1967, applicant was of the opinion that warehouse receipts, such as are allegedly involved herein, were not securities subject to its regulatory powers. (Letter dated July 6, 1967, from Arthur F. Mathews, Chief, Branch of Criminal Reference and Special Proceedings, Division of Trading and Markets, Securities and Exchange Commission, to Allan E. Backman, Executive Vice-President, National Better Business Bureau, Inc., attached to Brigadoon Reply Memorandum dated October 26, 1972.) As was pointed out in that letter, the basis for such position was that

> "[u]nder the present offers, the companies sell the whisky itself, rather than an investment contract based upon whisky. The purchaser owns the whisky,

> must insure it and warehouse it himself, and receives no investment advice from the sellers. Accordingly, no security is involved and no registration is required, as it was under the earlier types of investment."

The items in the subpoenas as to which this Court granted enforcement in its decision of September 5, 1972, were relevant and reasonable avenues of inquiry in the first instances to determine whether, under the practice followed by respondents, they did or did not sell the whiskey itself rather than an investment contract and whether the customer did or did not own, warehouse, and insure the whiskey and receive no investment advice from respondents. Having pursued these avenues, applicant would be in a position to seek prompt enforcement of the remaining two items of the subpoenas without incurring a charge of unnecessary and unreasonable harassment. In simple terms, applicant here, having invoked the power of the district court, would deny it the right to control the exercise of that power in an orderly and equitable fashion forgetting, perhaps, that the great demands of self-asserted "public interest" must still acknowledge the existence of individual rights. *See v. City of Seattle*, 387 U.S. 541, 544-45 (1967).

With respect to items 1 and 2 of the subpoenas, the Court granted enforcement but, in the light of the assertions by respondents as to the potential damage of their business, it noted that such damage "may be lessened by appropriate protective provisions in an order to be entered herein along the lines suggested by Respondent Leith-Moor" or "by direct communication by Respondents with the persons involved in these items." (Memorandum Opinion of September 5, 1972, at 7.) Applicant has made no attempt to submit or settle any order herein, nor has it suggested in any way some method of protecting against the possible destruction of a business over which it eventually may be found to have had no regulatory authority. Pending the settlement of an order herein by the prevailing party, we are more concerned with good faith than

with correct legal principles. The other matters raised by respondents are ones which are more appropriate for appellate determination.

The motions for reargument are granted and the prior decision of the Court is adhered to.

So ordered.

Dated: New York, New York
January 10, 1973

s/Charles H. Tenney
U.S.D.J.